NOTE: THIS MEMORANDUM SUPERCEDES THE MEMORANDUM DATED 11/28/07

Fair Political Practices Commission
MEMORANDUM

To: Chairman Johnson, Commissioners Hodson, Huguenin, Leidigh and Remy

From: Lawrence T. Woodlock, Senior Commission Counsel
Hyla P. Wagner, Senior Commission Counsel
Scott Hallabrin, General Counsel

Subject: Emergency Adoption of Regulation 18413 (Revised Draft)

Date: December 11, 2007

Proposed Commission Action and Recommendation: Adopt a *revised draft* of Regulation 18413 as an emergency regulation and approve publication of notice for permanent adoption.

Reason for Adoption: On November 14, 2007 the United States Court of Appeals for the Ninth Circuit issued its decision in *California ProLife Council, Inc. v. Randolph et al*. The opinion generally affirmed California's compelling interest in disclosure of the identities of persons that fund campaign advocacy published by groups like plaintiff ("CPLC"), a multi-purpose non-profit corporation organized and operating under Section 501(c)(4) of the Internal Revenue Code. But the court found that California had not proven that its interest in the disclosure of the source of campaign funding justified treatment of CPLC as a recipient committee, with its associated First Amendment burdens, if its campaign activities are limited to occasional independent expenditures supporting or opposing the qualification or passage of ballot measures.[1]

As explained in the prior memorandum dated November 28, 2007, the Ninth Circuit held that CPLC (and groups like CPLC) may still be required to disclose the identities of persons who donate to the entity's general treasury, from which payments are made for independent expenditures on ballot measures, but such a group may not be required to file a Statement of Organization as a recipient committee, to formally terminate that committee status when it ceases to make independent expenditures, to appoint a treasurer, file periodic campaign reports, or maintain the records required to be kept by a recipient committee.

After staff published the draft emergency regulation to implement this opinion, questions and observations from third parties indicated that the new regulation was not clear to all persons.

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[1] An "independent expenditure" is a payment made for a communication supporting or opposing the election of a clearly identified candidate or (of interest here) the qualification or passage of a clearly identified ballot measure, using language of express advocacy such as "support," "defeat," "vote for" and the like, when the communication is not made in coordination with or at the behest of the candidate or ballot measure proponent. A communication not couched in language of express advocacy is generally described as "issue advocacy," which is not regulated by the Act unless it is made at the behest of a candidate or measure proponent, in which case it is a "contribution."

Concluding that the public interest would be served by an expanded version of the proposed regulation that made its application and requirements more explicit, staff believes the earlier draft should be withdrawn and that the Commission adopt the attached draft instead.

Overview of the Proposed Regulation: The Act generally treats an entity that pays for an independent expenditure out of funds solicited from third parties as a "recipient committee." Classification as an "independent expenditure committee" has long been reserved for an entity that funds its independent expenditures out of its own resources. Since the court advises that we may not impose on groups like CPLC the incidental burdens of recipient committee status, the regulation offers groups like CPLC a reporting option that eliminates those burdens, so long as they do not engage in other activities (such as making contributions to candidates, or independent expenditures supporting or opposing the election of candidates) that would result in classification as a "recipient committee." The provisions of the draft regulation are organized as follows:

Subdivisions (a), (b) and (c) define, more explicitly than the prior draft, the non-profit corporations that may take advantage of the new "event-based reporting" rules described in Subdivison (d). Application of this regulation is limited, as before, to the kind of nonprofit corporation described by the court in its opinion.[2]

Subdivision (d) explains in detail the reporting requirements of a non-profit corporation described in the preceding subdivisions, which elects not to report as a "recipient" committee.

Subdivision (e) makes clear that the option for "event-based reporting" is not available to a nonprofit corporation that makes contributions or expenditures other than the independent expenditures described in subdivision (b)(2). Organizations thus qualifying as "recipient committees" under Section 82013(a) are required to report all contributions or expenditures as recipient committees.

To assist the regulated community in compliance with this new regulation, this memorandum includes a set of "Questions and Answers" similar to those frequently published by the Technical Assistance Division to supplement Commission regulations when inquiries from the regulated community demonstrate that further guidance would be useful. Because staff is proposing a regulation responding to a very recent judicial decision, it seems advisable to offer this kind of

[2] The court described CPLC as a non-profit corporation organized under Section 501(c)(4) to educate the public on abortion, infanticide, and euthanasia, whose "major purpose" is not the nomination or election of candidates or the passage or defeat of ballot measures. (Slip Opinion at p.14802.) After finding that California has properly tailored its rules for disclosure of funding sources for independent expenditures supporting or opposing ballot measures, the court next considered whether California had met its burden of showing that other "political action committee-like requirements" were sufficiently tailored to pass scrutiny when imposed "on a group like CPLC." (Slip Opinion at p. 14825.) Because the Ninth Circuit concluded that California had not met its burden in this regard, a curative emergency regulation must begin by describing entities "like CPLC" to which the regulation would apply.

practical assistance at an early stage, in the Question & Answer format often used to good effect by the Technical Assistance Division.

QUESTIONS AND ANSWERS

Question One: Our non-profit organization is not incorporated as a Section 501(c)(4) with the IRS. Can we use the event-based reporting procedure described in Regulation 18413?

Answer: No

Question Two: Our non-profit organization is incorporated as a Section 501(c)(4) corporation with the IRS and has exemption letters from both the IRS and the FTB. Can we use the event-based reporting procedure described in Regulation 18413?

Answer: Yes, assuming that your organization does not qualify as a "recipient committee" under Section 82013(a) by, for example, using funds donated to the organization's general treasury to make contributions to candidates, or independent expenditures supporting or opposing the election of candidates.

Question Three: Our non-profit organization is incorporated as a Section 501(c)(4) corporation with the IRS and has exemption letters from both the IRS and the FTB. Must we use the event-based reporting procedure described in Regulation 18413 if we already have a PAC and have been reporting our ballot-measure activity on the PAC's reports?

Answer: No. You are not required to change your current method of reporting. However, if you meet the eligibility requirements for event-based reporting, your organization may *elect* to report its ballot-measure independent expenditure activity in that manner.

Question Four: Our non-profit organization is incorporated as a Section 501(c)(4) corporation with the IRS and has exemption letters from both the IRS and the FTB. If we already have a PAC and have been reporting our ballot-measure activity on the PAC's reports, must we terminate our PAC if we choose to file event-based reports for our independent expenditure activities supporting or opposing ballot measures?

Answer : It depends. If your organization elects to file event-based reports for its ballot-measure independent expenditure activity, then it should terminate its PAC if the PAC only engages in independent expenditures relative to the qualification or passage of ballot measures. However, if the PAC also engages in candidate-related activities, or makes contributions to other entities for use in candidate or ballot measure campaigns, then you should maintain the PAC and continue reporting those activities on the PAC's reports.

Question Five: Our non-profit organization is incorporated as a Section 501(c)(4) corporation with the IRS and has exemption letters from both the IRS and the FTB. In 2006, we made for

the first time independent expenditures for or against ballot measures, totaling $25,000, which we disclosed on a Form 496, as required. If we make $50,000 in independent expenditures in 2008, how do we determine which donors we must disclose and the amount to be disclosed per donor, if we elect to use the event-based reporting method?

Answer: If you have received donations since the date of your 2006 expenditures, you will look at those donations and determine the amount that goes toward the $50,000 independent expenditures in 2008. Then apportion that amount using a reasonable accounting method to determine which donors to disclose and the respective amounts for each of them. One simple method would be a "last-in first-out ("LIFO") basis. But you may also use a percentage method. Be sure to keep records to establish the method used and how you determined the information reported.

Emergency Regulation Procedure: Under the statutes applicable to the Commission's adoption of regulations, the Commission may adopt an emergency regulation if, in any particular case the Commission makes a finding, including a statement of facts in writing describing the emergency, that the adoption of a regulation or order of repeal is necessary for the immediate preservation of the public peace, health and safety or general welfare. Included with the revised draft of Regulation 18413 and this memorandum is a memorandum detailing staff's recommended findings in support of the emergency adoption of the regulation. Once adopted, the regulation will remain in effect for 120 days, unless the regulation is permanently adopted in the interim. Staff proposes to bring this regulation to the Commission for permanent adoption within the 120-day period.

Fair Political Practices Commission
MEMORANDUM

To: Chairman Johnson, Commissioners Hodson, Huguenin, Leidigh and Remy

From: Scott Hallabrin, General Counsel

Subject: Findings for Adoption of Emergency Regulation 18413

Date: December 11, 2007

Commission Regulation 18312(c) requires the Commission, when adopting an emergency regulation, to include a statement of facts supporting the immediate adoption of the regulation and a statement that the regulation is necessary for the immediate preservation of the public peace, health and safety, or general welfare.

In the event the Commission votes to adopt proposed emergency Regulation 18413, staff recommends that it make the following findings before adopting the regulation:

1. In June 1974, California voters adopted Proposition 9, creating the Political Reform Act of 1974 ("the PRA"), by a vote of 70%.

2. The PRA, among other things, required the public reporting of campaign contributions and expenditures supporting and opposing ballot measures.

3. Among the findings and declarations supporting enactment of the PRA was the following: "The influence of large campaign contributions is increased because existing laws for disclosure of campaign receipts and expenditures have proved to be inadequate." (Gov. Code Sec. 81001(d).)

4. Among the enumerated purposes for the PRA was the following: "Receipts and expenditures in election campaigns should be fully and truthfully disclosed in order that the voters may be fully informed and improper practices may be inhibited." (Gov. Code Sec. 81002(a).)

5. Surveys have shown that California voters continue to be very interested in and desire campaign disclosure in ballot measure campaigns. As the United States Ninth Circuit Court of Appeals stated: "Researcher David Binder conducted a telephone survey from June 23-26, 2001. 'The goals of this project were to determine objectively, using established methods of scientific public opinion research, what sources of information regarding candidates and ballot measures are important to California voters.' According to Binder's findings, '[m]ore than seven of ten California voters (71%) state that it is

important to know the identity of the source and amount of campaign contributions to the ballot measure by both supporters and opponents, including unions, businesses or other interest groups." (*California Pro-Life Council v. Randolph* (9th Cir. 2007) Slip. Opn. at 14810, fn. 8; hereafter referred to as *CPLC II*.)

6. In *CPLC II*, the Ninth Circuit Court of Appeals further stated: "Professor Bruce Cain, a Professor of Political Science at the University of California, Berkeley, and Director of the Institute of Governmental Studies, added that 'there are several compelling reasons for such a requirement. Foremost among them is that the names groups give themselves for disclosure purposes can be, and frequently are, ambiguous or misleading.'" (*Id.* at 14810-11.)

7. The foregoing determinations by the Ninth Circuit Court of Appeals concur with the findings and purposes set forth in the PRA, as described in paragraphs 3 and 4 above.

8. Based upon the overwhelming evidence, the Ninth Circuit Court of Appeals in *CPLC II* concurred with the California voters who adopted Proposition 9 (the PRA), and stated: "[t]he purpose of the PRA is to inform voters of the identity of individuals and/or organizations who expend money in support of or in opposition to ballot measures." (*CPLC II* at 14802.) "We note that in the context of disclosure requirements, the government's interest in providing the electorate with information related to election and ballot measure issues is well-established. [Cites omitted.]" (*Id.* at 14810, fn. 8.)

9. On November 14, 2007, the Ninth Circuit Court of Appeals ruled in *CPLC II* that the PRA could not be applied to require certain non-profit groups like CPLC to comply with the full panoply of "political committee-like requirements" but could be applied to require CPLC and groups like CPLC to "disclose 'contributions,' as defined by the PRA" under existing Commission interpretations." (*CPLC II* at 14830.)

10. The decision in *CPLC II* has now become final in the Ninth Circuit Court of Appeals.

11. A statewide election is scheduled for February 5, 2008, less than eight weeks from now, and ballot measure campaigns are already under way for the seven ballot measures at that election that will, depending on the vote, either enact or reject very important legislation. It is anticipated that well over $100 million will be expended to influence voters on these ballot measures.

12. By restricting the manner in which the PRA applies to campaign reporting on ballot measure activities by organizations similar to the CPLC but providing no specific guidelines, the *CPLC II* decision has created confusion. If the Commission fails to take immediate action to clarify these campaign reporting responsibilities, the voters at the February 5, 2008 statewide general election are likely to be deprived of information, such

as the identity of persons who are making contributions and expenditures supporting or opposing measures that are on the ballot, which is critical to their votes for or against the measures.

13. Depriving voters at the February 5, 2008 statewide election of information about the identity of persons who are making contributions and expenditures supporting or opposing the measures on that ballot will result in great harm to the general public welfare.

14. Therefore, the Fair Political Practices Commission concludes that there is a compelling governmental interest in providing voters with information regarding those who make contributions and expenditures to influence the public's votes on ballot measure elections and the Commission must, of necessity, act expeditiously by adopting an emergency regulation to clarify the campaign reporting procedures and responsibilities under the PRA for non-profit organizations covered by the *CPLC II* decision.

Fair Political Practices Commission
MEMORANDUM

To: Chairman Johnson, Commissioners Hodson, Huguenin, Leidigh and Remy

From: Lawrence T. Woodlock, Senior Commission Counsel
Scott Hallabrin, General Counsel

Subject: Emergency Adoption of Regulation 18413

Date: November 28, 2007

Proposed Commission Action and Recommendation: Adopt Regulation 18413 as an emergency regulation and approve publication of notice for permanent adoption of the regulation.

Reason for Adoption: On November 14, 2007 the United States Court of Appeals for the Ninth Circuit issued its decision in *California ProLife Council, Inc. v. Randolph et al*. A copy of the slip opinion is attached. The opinion generally affirmed California's compelling interest in disclosure of the identities of persons that fund campaign advocacy published by groups like plaintiff ("CPLC"), a multi-purpose non-profit corporation organized and operating under Section 501(c)(4) of the Internal Revenue Code. However, the court found that California had not demonstrated that its interest in the disclosure of the source of campaign funding justified treatment of CPLC as a recipient committee, with its associated First Amendment burdens, if its campaign activities are limited to occasional independent expenditures supporting or opposing the qualification or passage of ballot measures.[3]

Under this opinion, CPLC (and groups like CPLC) may still be required to disclose the identities of persons who donate to the entity's general treasury, from which payments are made for independent expenditures on ballot measures, but such a group may not be required to file a Statement of Organization as a recipient committee, to formally terminate that committee status when it ceases to make independent expenditures, to appoint a treasurer, file periodic campaign reports, or maintain the records required to be kept by a recipient committee.

To align the Act with the court's ruling as litigation continues, staff proposes a regulation that would eliminate what the court found to be requirements that may not be imposed on CPLC and similar groups. In the absence of a regulation implementing the court's opinion, there is likely to

[3] An "independent expenditure" is a payment made for a communication supporting or opposing the election of a clearly identified candidate or (of interest here) the qualification or passage of a clearly identified ballot measure, using language of express advocacy such as "support," "defeat," "vote for" and the like, when the communication is not made in coordination with or at the behest of the candidate or ballot measure proponent. A communication not couched in language of express advocacy is generally described as "issue advocacy," which is not regulated by the Act unless it is made at the behest of a candidate or measure proponent, in which case it is a "contribution."

be some uncertainty regarding the current state of the law, which should be addressed promptly in light of the upcoming February and June elections.
An emergency regulation is the only vehicle by which the Commission can conform its rules to the court's opinion in advance of the upcoming February election. Staff anticipates that it will be able to present a regulation, vetted by a fuller rulemaking process, for permanent adoption at the monthly Commission meeting in February or March, 2008.

Overview of the Emergency Regulation: The Act generally treats an entity that pays for independent expenditures out of funds solicited from third parties as a "recipient committee." Classification as an "independent expenditure committee" has long been reserved for an entity that funds its independent expenditures out of its own resources. Since the court advises that we may not impose on groups like CPLC the incidental burdens of recipient committee status, the regulation eliminates those burdens by classifying CPLC as a kind of independent expenditure committee, so long as it doesn't engage in other activities that would result in its classification as a "recipient committee." The provisions of the draft regulation are explained in detail below.

Subdivision (a) describes a new subset of the "independent expenditure committee" defined at Section 82013(b), consisting of a multi-purpose non-profit corporation organized under Section 501(c)(4), which makes independent expenditures supporting or opposing ballot measures, but does not otherwise qualify as a "recipient committee" defined at Section 82013(a). Application of this regulation is thus limited to the kind of entity discussed by the court in its opinion.[4]

Subdivision (a) offers a schematic description of a group like CPLC. It is important to highlight entities that are *not* within the scope of this regulation. Because the regulation applies to "multi-purpose groups," it should *not* apply to a non-profit entity used to funnel money into political campaigns, when political campaigns would become an entity's "major purpose."[5] The District Court pointed out that a "major purpose" test, if the term refers to a "purpose" controlling more than half of a group's budget, would permit very large multi-purpose non-profit groups to swamp state and local elections without spending more than half their resources to do so. Experience may teach that this regulation should specify another characteristic of CPLC that was urged throughout the litigation (its relatively small size) in support of a monetary cap on the level of political activity by a group with reduced administrative obligations under this regulation. Administrative burdens shrink as economies of scale expand in groups distributing very large

[4] The court described CPLC as a non-profit corporation organized under Section 501(c)(4) to educate the public on abortion, infanticide, and euthanasia, whose "major purpose" is not the nomination or election of candidates or the passage or defeat of ballot measures. (Slip Opinion at p.14802.) After finding that California has properly tailored its rules for disclosure of funding sources for independent expenditures supporting or opposing ballot measures, the court next considered whether California had met its burden of showing that other "political action committee-like requirements" were sufficiently tailored to pass scrutiny when imposed "on a group like CPLC." (Slip Opinion at p. 14825.) Because the Ninth Circuit concluded that California had not met its burden in this regard, a curative emergency regulation must begin by describing entities "like CPLC" to which the regulation would apply.

[5] Subdivision (c) provides that such a funneling operation would result in characterization of the entity as a recipient committee, when the facts betray an intent to use a large influx of money to fund electoral advocacy.

sums of money, and the Ninth Circuit did not discuss the tailoring appropriate to a group spending $500,000 or $1,000,000 per year in independent expenditure campaigns.
Subdivision (b) creates an exception to the "one bite of the apple" rule codified at Regulation 18215(b)(1). This rule imputes knowledge to a group's donors that subsequent donations will be used for political purposes, once the group has used its donor-funded treasury to make political expenditures or contributions of $1,000 or more in a calendar year. In such cases, a portion of subsequent "donations" are treated as "contributions" to the group, which qualify it as a recipient committee under Section 82013(a) if the incoming contributions amount to $1,000 or more in a calendar year. Subdivision (b) of the proposed regulation *exempts* a multi-purpose non-profit corporation from the effect of this rule, if its political expenditures are confined to "independent expenditures" supporting or opposing ballot measures. The final sentence warns that other kinds of political activities may still qualify the group as a recipient committee.

An exception to the committee qualification provision of Regulation 18215(b)(1) is necessary to ensure that the independent expenditure committee described in subdivision (a) does not become a recipient committee by operation of the "one bite of the apple" rule.

Subdivision (c) is a specific reminder that an entity meeting the criteria of subdivision (a) can nonetheless qualify as a recipient committee if it accepts other "contributions." If an entity qualifies as a recipient committee for activities unrelated to its independent expenditures on ballot measures, it is not an "independent expenditure committee" described in subdivision (a) of the proposed regulation, and would report all of its activities as a recipient committee.

Subdivision (d) describes the rules under which an independent expenditure committee meeting the criteria of subdivision (a) would report its independent expenditures. The rules stated in this subdivision are the same as those applicable to independent expenditure committees generally, as defined under Section 82013(b).

The language of the draft regulation does not make it clear that an entity meeting the criteria of subdivision (a) of the draft regulation may *choose* to accept status as a recipient committee, and to file its reports as a recipient committee, if this is more convenient. If it appears that there is demand for such an option, the regulation can be modified at the final adoption stage to make the option more clear. It was staff's intent in this draft to provide a new option to qualifying entities, and not to require that such organizations alter their accustomed compliance practices.

Subdivision (e) introduces two clarifications to the foregoing rules. Independent expenditure committees generally report their independent expenditures only once, when they are "made."[6] However, if the entity controls a recipient committee (i.e. a PAC), it is also required to report independent expenditures from the corporate treasury on the PAC's regularly scheduled reports. Such a rule imposes little or no additional administrative burden on a non-profit corporation that

[6] An "independent expenditure" is considered to have been made on the date the communication is mailed, broadcast, or otherwise disseminated to its intended audience.

operates a recipient committee, but it serves the public interest well by gathering in one place the political expenditures of two intimately related entities.

In staff's opinion, the draft regulation effectively addresses the Ninth Circuit's concerns on the "tailoring" of the Act's rules to groups matching the description of CPLC, which the court used as the basis of its legal analysis. Specifically, by treating such groups as independent expenditure committees, the regulation eliminates all of the "political action committee-like requirements" unrelated to disclosure of funding sources for independent expenditures. The proposed regulation requires "event-based" reporting of an independent expenditure on a form already in use for independent expenditure committees, but does *not* require such groups to file a Statement of Organization as a recipient committee, and by implication to file a Termination Statement. Nor is this kind of committee required to appoint a treasurer, to file periodic reports like a recipient committee, or to keep the books and records required of a recipient committee. The only obligation imposed on a group like CPLC will be an event-based report of its independent expenditures, identifying persons who donated funds from which the expenditure was paid on a simple "last-in, first-out" methodology.

Conclusion: There may be some danger that persons will attempt to exploit this regulation by creating non-profit groups, or by using existing groups, to serve as conduits to channel large sums of money into ballot measure campaigns. Staff believes that such activities would be a violation of the Act. First, because the evident motivation would properly classify the incoming funds as "contributions," qualifying the recipient as a recipient committee and, second, because the large-scale use of newly-arrived funds to fuel ballot measure advocacy would establish such advocacy as a "major purpose" of the non-profit entity. The Ninth Circuit appears to have based its legal analysis on CPLC's assertion that its major purposes did not include ballot measure advocacy. A group that *does* exhibit such a purpose is not therefore a "group like CPLC."

Emergency Regulation Procedure: Under the statutes applicable to the Commission's adoption of regulations, the Commission may adopt an emergency regulation if, in any particular case the Commission makes a finding, including a statement of facts in writing describing the emergency, that the adoption of a regulation or order of repeal is necessary for the immediate preservation of the public peace, health and safety or general welfare. In the present case, the Ninth Circuit Court of Appeals has issued an opinion finding that certain of the Act's committee formation and disclosure provisions governing multi-purpose non-profit corporations place burdens on First Amendment rights. To ensure that the voters continue to receive full and timely information on the sources of money spent in ballot measure campaigns, it is necessary to adopt an emergency regulation describing in detail the entities to which the court's ruling applies, and the campaign disclosure obligations to which those entities remain subject. Once adopted, the regulation will remain in effect for 120 days, unless the regulation is permanently adopted in the interim. Staff proposes to bring this regulation to the Commission for permanent adoption within the 120-day period.